INDEX

	Page
Opinions below	1
Jurisdiction	2
Question presented	2
Statute and regulations involved	2
Statement	2
Specification of errors to be urged	13
Reasons for granting the writ	14
Conclusion	18
Appendix	19

CITATIONS

Cases:	
Bert v. *Helvering*, 92 F. (2d) 491	17
Burk-Waggoner Assn. v. *Hopkins*, 269 U. S. 110	15, 16, 17
Commissioner v. *Highlands E.-L. Subd., etc.*, 88 F. (2d) 355, certiorari denied, 302 U. S. 691	18
Commissioner v. *Vandegrift Realty Co.*, 82 F. (2d) 387	18
Hecht v. *Malley*, 265 U. S. 144	15
Helvering v. *Coleman-Gilbert*, 296 U. S. 369	15, 16, 17
Helvering v. *Combs*, 296 U. S. 365	15, 16, 17, 18
Monrovia Oil Co. v. *Commissioner*, 83 F. (2d) 417	17
Morrissey v. *Commissioner*, 296 U. S. 344	15, 16, 17
Swanson v. *Commissioner*, 296 U. S. 362	15, 16, 17
Thrash Lease Trust v. *Commissioner*, 99 F. (2d) 925, certiorari denied, 306 U. S. 654	14
Title Insurance & Trust Co. v. *Commissioner*, 100 F. (2d) 482	17
United States v. *Trust No. B. I. 35*, 107 F. (2d) 22	18
Wellston Hills Syndicate Fund v. *Commissioner*, 101 F. (2d) 924	17
Wholesalers Adjustment Co. v. *Commissioner*, 88 F. (2d) 156	17
Statute:	
Revenue Act of 1932, c. 209, 47 Stat. 169:	
Sec. 13	19
Sec. 52	19
Sec. 1111 (U. S. C., Title 26, Sec. 1696)	20
Miscellaneous:	
Treasury Regulations 77:	
Art. 1311	20
Art. 1312	20
Art. 1313	21
Treasury Regulations 86:	
Art. 801–1	22
Art. 801–2	22, 23
Art. 801–3	23
Art. 801–4	26
Art. 801–5	27

240625—40——1

In the Supreme Court of the United States

OCTOBER TERM, 1940

No. —

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

HORSESHOE LEASE SYNDICATE

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Fifth Circuit entered in the above entitled cause on March 26, 1940.

OPINIONS BELOW

The unpublished memorandum opinion of the Board of Tax Appeals is printed in the record at pages 13 to 24, inclusive. The opinion of the Circuit Court of Appeals is reported in 110 F. (2d) 748.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered March 26, 1940. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the group associated together and doing business under the name of Horseshoe Lease Syndicate was, during the taxable year involved, an "association" within the meaning of Section 1111 (a) (2) of the Revenue Act of 1932 and as such subject to income tax as a corporation during the year.

STATUTE AND REGULATIONS INVOLVED

The pertinent provisions of the statute and regulations involved are printed in the Appendix, *infra*, pp 19–27.

STATEMENT

The Horseshoe Lease Syndicate, hereafter sometimes referred to as the taxpayer, filed a Partnership Return of Income for the year 1932, disclaiming any liability for federal income tax. (R. 13, 85, 127–128.) Thereafter the Commissioner of Internal Revenue determined that during the year involved the Syndicate was doing business as an association within the meaning of Section 1111 (a) (2) of the Revenue Act of 1932, and as such was subject to income tax as a corporation. He therefore asserted the deficiency in a tax here in contro-

versy (R. 6, 13–14, 146–150), and a petition for review was filed with the United States Board of Tax Appeals (R. 6–9). The proceeding was submitted to the Board upon a stipulation of facts (R. 81–151) which was incorporated by reference in the findings of fact made by the Board (R. 14), and upon oral testimony adduced at the hearing before the Board (R. 60–80). In its memorandum opinion the Board summarized the facts as follows (R. 14–23):

On January 28, 1931, W. J. Brightwell, and others, the joint owners and claimants of an interest in a tract of about 65 acres of land known as the Brightwell place located in Rusk County, as parties of the first part, and J. Edgar Finley, P. T. Fullwood, and the Patterson Drilling Company, a Texas corporation, as parties of the second part, entered into an agreement relating to that land. Such agreement provided, *inter alia,* that after the survey and platting of the land the first parties would execute an oil and gas lease to the second parties covering a parcel 600 feet by 660 feet in the tract subject to a ⅛th royalty and a yearly rental of $1 per acre; that the second parties would organize a syndicate having 350 units, par value of $100 each, for the purpose of drilling wells on the 600 foot by 660 foot tract, and marketing the products therefrom, and would, as balance of the consideration for said lease, deliver 35 of such units to the first parties; that the second parties would commence drilling within a specified time, complete and

equip a well at their own expense, and under certain conditions would drill and equip a second well; and that an escrow agent would deliver the executed lease to the second parties after they had spudded in the first well. Such agreement was executed and acknowledged by all of the necessary parties thereto and was recorded in the deed records of Rusk County, Texas. Due to certain conditions which arose, some of the provisions of that agreement, immaterial here, were not carried out. (R. 14–15.)

Pursuant to the agreement of January 28, 1931, W. J. Brightwell and others, as lessors, executed and delivered in escrow an oil and gas lease, dated February 9, 1931, to J. Edgar Finley, P. T. Fullwood, and the Patterson Drilling Company, as lessees. The lease was for a term of five years and as long thereafter as oil, gas, or other mineral was produced from the leased premises. The lease was duly signed and acknowledged by the proper parties and was duly recorded on April 25, 1931, in the deed records of Rusk County, Texas. The lease embraced the northwest corner, described by metes and bounds, of the Brightwell 65 acre tract, and under the terms thereof the lessors reserved a royalty of 1/8 of the oil produced and saved and certain royalties on gas and other minerals. The lessees were, under the agreement of January 28, 1931, obligated to drill and equip at least one well. (R. 15.)

On May 16, 1931, Finley, Fullwood, and W. A. Patterson, the latter as an officer of the Patterson

Drilling Company, filed, in Rusk County, Texas, under the "Assumed Name Law of Texas," a certificate of ownership under the assumed name of "Horseshoe Lease Syndicate." That name was adopted to identify the lease. (R. 15–16.)

Finley, Fullwood, and the Patterson Drilling Company divided their joint interest in the lease into 350 fractional parts, and pursuant to the agreement of January 28, 1931, they conveyed 35/350ths interests to the above mentioned original lessors, which interests were to be non-assessable for any expenses incident to the drilling of the wells or the marketing of oil or gas produced therefrom. Also, prior to January 1, 1932, and as the owners thereof, they sold numerous undivided fractional interests in the lease for $100 for each 1/350th interest for the purpose of financing the drilling and equipping of one well, retaining a large number of such interests for themselves. They executed and delivered an assignment for each such fractional interest in the following form (R. 16–21):

ASSIGNMENT OF OIL AND GAS LEASE

> WHEREAS, J. Edgar Finley, P. T. Fullwood, Patterson Drilling Co. (a corporation), are the owners of oil, gas and mining leases covering the following described tract of land situated in Rusk County, Texas, to-wit:
>
> * * * * *
>
> NOW THEREFORE, * * * the undersigned, the present owners of the said lease

and all rights thereunder or incident thereto, do hereby bargain, sell, transfer, assign and convey unto ---------- an undivided ---------- interest in and to all of the right, title and interest of the original lessee, * * *.

* * * * *

1. In consideration of the grantee, herein above named, purchasing this assignment and the leasehold property herein conveyed, J. Edgar Finley, P. T. Fullwood, Patterson Drilling Co. hereby contract and agree to do the following things, to-wit:

(a) To drill at their own cost and expense, one well on the lease above described; said well to be drilled to a depth of 3,700 feet unless granite in solid formation in its regular place is encountered at a lesser depth and in such quantities as to render it impenetrable; or unless oil or gas in paying quantities be encountered at a lesser depth. The said owners shall have the right to drill an additional well on said lease, if in their judgment it appears to be to the best interests of the owners of this lease; and the expense of drilling and equipping such additional well and all equipment necessary for said lease, shall be paid out of the funds received from the sale of oil or gas produced from said lease; it being specifically understood that J. Edgar Finley, P. T. Fullwood and Patterson Drilling Company only contract to drill one well; but they may drill an additional well, if in their judgment it appears to be to the best interests of all the owners

of said lease. J. Edgar Finley, P. T. Fullwood and Patterson Drilling Co. (a Corporation), reserve the right, and they are also expressly empowered to borrow money for the purpose of drilling and equipping such additional well, and pledge and encumber by giving a lien thereon, said lease, in whole or in part, for the purpose of securing the payment of all money so borrowed.

2. In consideration for J. Edgar Finley, P. T. Fullwood and Patterson Drilling Co. doing the things set out and stipulated in the paragraph numbered "1" above and in subdivision "a" thereof, the owner and holder of this assignment agrees that J. Edgar Finley, P. T. Fullwood and Patterson Drilling Co. shall operate said lease above described for the benefit of all the parties interested in said lease; and shall collect for all pipe line runs of oil from said lease, and likewise, collect all money to be received from the sale of gas from said lease; and after having paid all proper operating expenses, shall distribute and pay to the owners of said lease, such proportion of the remaining proceeds as their respective interests in said lease shall entitle them to receive, according to the proportionate part of said lease they then own.

3. It is further agreed by the parties hereto that the undersigned J. Edgar Finley, P. T. Fullwood and Patterson Drilling Co. shall have the power at any time, in their discretion, to sell and dispose of all or any part of the above described lease-hold prop-

erty on such terms and conditions and at such price as in their judgment shall seem best and proper, and the said J. Edgar Finley, P. T. Fullwood and Patterson Drilling Co., as a part of this sale, hereby reserve the power and right to make such sale or sales of all or any part of said property, and to transfer, convey, and assign the same, and as an incident thereto, they shall execute and deliver all such written instruments as may be necessary or required to properly and legally convey and assign good title thereto, to the purchaser or purchasers thereof. And the said J. Edgar Finley, P. T. Fullwood and Patterson Drilling Co. are, for the purpose of making such sale or sales, fully and completely authorized and empowered to sign the name of the grantee herein to any and all instruments that may be necessary to be executed and in all other respects to act in said grantee's place and stead as said grantee's attorney in fact, executing, acting and delivering such written instruments and muniments of title the same as said grantee could do if personally present and executing and delivering the same in person, and in accepting and buying this assignment, the grantee herein does so with the express understanding that the said J. Edgar Finley, P. T. Fullwood and Patterson Drilling Co., as above stipulated and provided, may act as attorney in fact for said grantee as above set out, the said grantee hereby ratifying and confirming all such

lawful acts as the said J. Edgar Finley, P. T. Fullwood and Patterson Drilling Co. shall do or cause to be done by virtue thereof. It is expressly understood and agreed, however, that when said leasehold property or any part thereof shall have been sold as herein provided, the said J. Edgar Finley, P. T. Fullwood and Patterson Drilling Co. shall receive and distribute to each of the parties owning an interest in said lease-hold property or any part thereof, such proportionate part of the net proceeds derived from said sale as each of said parties shall be entitled to receive, according to the interest each of the parties respectively owns in said lease-hold property or part thereof. It is further agreed by and between the grantor and grantee herein that this instrument is to be effective as an assignment, transfer and conveyance of the interest herein described only when signed and acknowledged by both the grantor and grantee herein.

J. Edgar Finley, P. T. Fullwood and Patterson Drilling Co. hereby reserve the right to pay all money due to the owner of the interest hereby assigned to the grantee herein unless they shall have received notice that the interest hereby assigned has been sold and assigned by the grantee herein to some other person. All subsequent assignees of the interest herein assigned shall take said interest subject to and be bound by the terms, covenants, agreements and reservations herein contained.

IN WITNESS WHEREOF, the undersigned owner and grantor has signed and sealed this instrument this ____ day of _____ A. D. 19__.

_____

_____

PATTERSON DRILLING CO.

_____ [SEAL]

Grantee

By _____

Grantors.

There was no restriction on the conveyance or reassignment by the assignees of such fractional leasehold interests and in fact many of such interests were reassigned by the original assignees and in such instances the operation of the leased premises was continued uninterrupted by such transfers which were made subject to the agreement set out in the original assignments. (R. 21.)

Finley, Fullwood, and the Patterson Drilling Company secured a drilling permit issued to the Horseshoe Lease Syndicate by the proper authorities of the State of Texas. Pursuant to their agreement with the lessors and the agreement contained in the assignment to each purchaser of a fractional interest, they drilled and equipped the first well on the leased premises at their own expense. The driller was paid in part by assignment by Finley, Fullwood, and Patterson Drilling Company of a fractional interest in the lease out of their remaining joint interest therein, and the equipment was paid for by each contributing the sum of $2,250 out of his own funds. A second well was drilled in

1933, payment for which was made out of the proceeds of oil and gas therefrom. (R. 21.)

During a period including the taxable year, Finley, Fullwood, and Patterson, the latter as an officer and on behalf of the Patterson Drilling Company, operated the leased premises and arranged for the sale of the oil produced therefrom and the distribution of the proceeds therefrom in accordance with the terms of their agreement with the lessors and their separate agreements with each purchaser of a fractional interest. Such operations were on behalf of the various co-owners of fractional interests in the leased premises, including themselves, and no sale of that lease nor purchase of any additional lease was made by Finley, Fullwood, and the Patterson Drilling Company on behalf of such owners during the taxable year. Finley, Fullwood, and Patterson kept their records at various places and used convenient mailing addresses until they employed an accountant in June, 1931, and thereafter their books and records were kept in that accountant's office. There was no declaration of trust in connection with the Horseshoe Lease Syndicate or the leased premises, but to avoid the necessity of Finley, Fullwood, and Patterson all signing checks, those three designated Fullwood as trustee to sign such checks. (R. 21–22.)

Pursuant to a division order covering a 7/8ths interest in the leased premises and signed by D. M. Finley, J. Edgar Finley, P. T. Fullwood, and the

Patterson Drilling Company by W. A. Patterson, the monthly checks from the pipe line company for oil purchased were made payable to those four parties, who endorsed such checks, which were then deposited in the Citizens National Bank of Henderson, Texas, in an account captioned "Horseshoe Lease Syndicate". After deducting the operating expenses, including the salaries paid to the auditor, a lease superintendent, and workman, the monthly net proceeds from the oil runs were distributed *pro rata* each month to the owners of fractional interests by checks drawn on the bank account of the "Horseshoe Lease Syndicate", such checks being signed, "Horseshoe Lease Syndicate by P. T. Fullwood, Trustee". No surplus in excess of anticipated expenses was ever maintained. (R. 22–23.)

During 1932 there were numerous owners of fractional interests in the leased premises, including Finley, Fullwood, and the Patterson Drilling Company, the latter three having retained a large number of unsold fractional interests therein. Certificates or evidences of their interests other than the above mentioned assignments and the conveyances were never issued to them, or any of them. There was no limitation upon the personal liability as tenants in common, of the various co-owners of the lease, except as to the original lessors as the Owners of 35/350ths interests therein. They never held any meetings, had no by-laws, paid no rent for office space, never borrowed any money, never made any declaration of trust, and they were never

consulted with reference to the operation of the leased premises, except that written consent for the drilling of the second well was obtained from each owner of a fractional interest in the lease. (R. 23.)

The Board concluded, on the basis of the foregoing statement, that the Horseshoe Lease Syndicate was not doing business as an "association" during the year 1932 within the meaning of the statute and that it was therefore not taxable as a corporation. (R. 23–24.) The Circuit Court of Appeals affirmed.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the question whether the Horseshoe Lease Syndicate was taxable as a corporation during the year involved is a question of fact, and in failing to hold that the question is a question of law.

2. In holding, on its assumption that the question is one of fact, that the Board of Tax Appeals found as a fact that the Syndicate was not an association taxable as a corporation for the year involved.

3. In holding, on its assumption that the question is one of fact, that the evidence supports the Board's finding that the Syndicate is not an association taxable as a corporation.

4. In failing to hold as a matter of law that the Horseshoe Lease Syndicate was, during the year

1932, doing business as an association as that term is used in Section 1111 (a) (2) of the Revenue Act of 1932, and as such subject to the federal income tax imposed on corporations.

5. In affirming the decision of the Board of Tax Appeals.

REASONS FOR GRANTING THE WRIT

The decision below conflicts in several respects with decisions in other circuits as well as with decisions of this Court. Moreover, the question presented is an important one in the administration of the revenue acts because the device employed in this case is common in the financing and development of oil properties, and the question presented is of frequent recurrence.

1. The decision below is in substantial conflict with *Thrash Lease Trust* v. *Commissioner*, 99 F. (2d) 925 (C. C. A. 9th), certiorari denied, 306 U. S. 654. There an arrangement similar to the arrangement in the instant case was entered into for the development and exploitation of an oil and gas lease in Texas. The lease was assigned to one Gordon Macmillan, as trustee, and the development of the property and assignment of interests were carried out in much the same manner as those details were carried out in the instant case. Percentage interests were assigned to many persons, some of the interests purporting to be interests in the oil and gas and some purporting to be interests in the lease. There were some variations in the

terms of the assignments. All were transferable and some actually were transferred. All business transactions and operations of the well were conducted, and the net proceeds from operation were distributed by Gordon Macmillan and his father in much the same manner as the business of the Horseshoe Lease Syndicate and the distribution of its profits were carried out by Finley, Fullwood, and the Patterson Drilling Company. In that case the court held that the group operating the lease involved constituted an "association" taxable as a corporation.

2. The decision below conflicts with the principles announced by this Court in *Morrissey* v. *Commissioner*, 296 U. S. 344; *Swanson* v. *Commissioner*, 296 U. S. 362; *Helvering* v. *Combs*, 296 U. S. 365; *Helvering* v. *Coleman-Gilbert*, 296 U. S. 369; and *Burk-Waggoner Assn.* v. *Hopkins*, 269 U. S. 110. It has been clearly established that a cooperative business enterprise qualifies as an "association" where there is centralized management and where the beneficial interests are transferable without affecting the continuity of the enterprise. *Morrisey* v. *Commissioner, supra*, at 356–360. And it is equally clear that other corporate characteristics such as a voice in the management of the group affairs by the participants,[1] formal evidence of

[1] *Hecht* v. *Malley*, 265 U. S. 144; *Morrissey* v. *Commissioner*, 296 U. S. 344, 358; *Helvering* v. *Combs*, 296 U. S. 365, 368.

beneficial interest,[2] election of officers, formal meetings, by-laws and the like,[3] while serving to emphasize the corporate analogy in individual cases, are not essential to classification of the group as an association. Nor is it material that the enterprise may be limited to a single project such as the operation of one oil well.[4] And, the classification of an enterprise as an association "is not affected by the fact that, under the law of a particular State, the association cannot hold title to property, or that its shareholders are individually liable for the association's debts, or that it is not recognized as a legal entity." *Burk-Waggoner Assn.* v. *Hopkins*, 269 U. S. 110, 114.

In the instant case all of the essential corporate attributes are present. The lessees of the oil and gas lease and the holders of participating interests were "associates." They had entered into a joint enterprise for the transaction of business. Cf. *Morrissey* v. *Commissioner*, 296 U. S. 344, 356. The participating interests were freely assignable, and actually were assigned, thus assuring continuity of the life of the enterprise. And management of group affairs was, by reason of the undertakings, reservations, and powers granted to the lessees or operators by the terms of the purported assignment

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[2] *Morrissey* v. *Commissioner*, 296 U. S. 344, 358; *Helvering* v. *Coleman-Gilbert*, 296 U. S. 369.

[3] *Swanson* v. *Commissioner*, 296 U. S. 362, 364; *Helvering* v. *Combs*, 296 U. S. 365, 368; *Helvering* v. *Coleman-Gilbert*, 296 U. S. 369, 372–373.

[4] *Helvering* v. *Combs*, 296 U. S. 365, 368.

of undivided interests in the oil and gas lease, centralized in the three promoters.

Since all of the essential corporate characteristics were present in the instant case the decision below holding that the Syndicate is not an association taxable as a corporation is in substantial conflict with the decisions of this Court in *Burk-Waggoner Assn.* v. *Hopkins, supra; Morrissey* v. *Commissioner, supra; Swanson* v. *Commissioner, supra; Helvering* v. *Combs, supra;* and *Helvering* v. *Coleman-Gilbert, supra.*

Moreover, the decision below is in conflict with a number of cases in other circuits to the extent that it fails to apply the principles established by the foregoing decisions of this Court. *Monrovia Oil Co.* v. *Commissioner,* 83 F. (2d) 417 (C. C. A. 9th); *Wholesalers Adjustment Co.* v. *Commissioner,* 88 F. (2d) 156 (C. C. A. 8th); *Bert* v. *Helvering,* 92 F. (2d) 491 (App. D. C.); Title Insurance & Trust Co. v. *Commissioner,* 100 F. (2d) 482 (C. C. A. 9th); *Wellston Hills Syndicate Fund* v. *Commissioner,* 101 F. (2d) 924 (C. C. A. 8th).

3. Whether the Horeshoe Lease Syndicate is an association within the statutory definition was treated by the court below as a question of fact, and it limited its review simply to an examination of whether there was "substantial evidence to support" what it described as "the finding" of the Board of Tax Appeals. In so limiting the scope of review, the decision below is in direct conflict with a number of decisions which treat the ques-

tion as one of law, and in each one of which the judgment of the lower tribunal was reversed. E. g. *Commissioner* v. *Vandegrift Realty Co.*, 82 F. (2d) 387 (C. C. A. 9th); *Commissioner* v. *Highlands E.-L. Subd., etc.*, 88 F. (2d) 355 (C. C. A. 7th), certiorari denied, 302 U. S. 691; *United States* v. *Trust No. B. I. 35*, 107 F. (2d) 22 (C. C. A. 9th); *Helvering* v. *Combs*, 296 U. S. 365.

4. This case involves an issue of considerable importance in the administration of the income tax statutes. The question presented is a frequently recurring one, since the method of operation adopted by the parties interested in this lease is used extensively throughout the oil producing sections of the country. Many cases are pending before the Bureau of Internal Revenue, the Board of Tax Appeals, and the courts involving the same question with respect to similar joint undertakings. It is important, therefore, that this Court settle the application of established principles to this type of case.

CONCLUSION

Wherefore, it is respectfully submitted that this petition should be granted.

FRANCIS BIDDLE,
Solicitor General.

JUNE, 1940.

APPENDIX

Revenue Act of 1932, c. 209, 47 Stat. 169:

SEC. 13. TAX ON CORPORATIONS.

(a) *Rate of Tax.*—There shall be levied, collected, and paid for each taxable year upon the net income of every corporation, a tax of 13¾ per centum of the amount of the net income in excess of the credit against net income provided in section 26.

* * * * *

SEC. 52. CORPORATION RETURNS.

(a) *Requirement.*—Every corporation subject to taxation under this title shall make a return, stating specifically the items of its gross income and the deductions and credits allowed by this title. The return shall be sworn to by the president, vice president, or other principal officer and by the treasurer or assistant treasurer. In cases where receivers, trustees in bankruptcy, or assignees are operating the property or business of corporations, such receivers, trustees, or assignees shall make returns for such corporations in the same manner and form as corporations are required to make returns. Any tax due on the basis of such returns made by receivers, trustees, or assignees shall be collected in the same manner as if collected from the corporations of whose business or property they have custody and control.

* * * * *

SEC. 1111. DEFINITIONS.

(a) When used in this Act—

(1) The term "person" means an individual, a trust or estate, a partnership, or a corporation.

(2) The term "corporation" includes associations, joint-stock companies, and insurance companies.

(3) The term "partnership" includes a syndicate, group, pool, joint venture, or other unincoporated organization, through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of this Act, a trust or estate or a corporation; and the term "partner" includes a member in such a syndicate, group, pool, joint venture, or organization.

* * * * *

(8) The term "stock" includes the share in an association, joint-stock company, or insurance company.

(9) The term "shareholder" includes a member in an association, joint-stock company, or insurance company.

* * * * *

(U. S. C., Title 26, Sec. 1696.)

Treasury Regulations 77, promulgated under the Revenue Act of 1932:

ART. 1311. *Person.*—The Act recognizes four classes of persons—individuals, trusts and estates, partnerships, and corporations. Corporations include associations, joint-stock companies, and insurance companies, but not partnerships properly so called. A taxpayer is any person subject to a tax imposed by the Act.

ART. 1312. *Association.*—Associations and joint-stock companies include associations,

common law trusts, and organizations by whatever name known, which act or do business in an organized capacity, whether created under and pursuant to State laws, agreements, declarations of trust, or otherwise, the net income of which, if any, is distributed or distributable among the shareholders on the basis of the capital stock which each holds, or, where there is no capital stock, on the basis of the proportionate share or capital which each has or has invested in the business or property of the organization. A corporation which has ceased to exist in contemplation of law but continues its business in quasi-corporate form is an association or corporation within the meaning of section 1111.

ART. 1313. *Association distinguished from partnership.*—An organization, the membership interests in which are transferable and the business of which is conducted by trustees or directors and officers without the active participation of all the members as such, is an association and not a partnership. The term "partnership" includes a syndicate, group, pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of the Act, a trust or estate or a corporation; and the term "partner" includes a member in such a syndicate, group, pool, joint venture, or organization. Organizations which have a fixed capital stock divided into shares represented by certificates transferable only upon the books of the company, which manage their affairs by a board of directors or executive officers, and which conduct their business in the general form and mode of

corporations are joint-stock companies or associations within the meaning of the Act even though under State law such organizations are technically partnerships.

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

ART. 801–1. *Classification of taxables.*—For the purpose of taxation the Act makes its own classifications and prescribes its own standards of classification. Local law is of no importance in this connection. Thus a trust may be classed as a trust or as an association (and, therefore, as a corporation), depending upon its nature or its activities. (See article 801–3.) The term "partnership" is not limited to the common law meaning of partnership, but is broader in its scope and includes groups not commonly called partnerships. (See article 801–4.) The term "corporation" is not limited to the artificial entity usually known as a corporation, but includes also an association, a trust classed as an association because of its nature or its activities, a joint-stock company, an insurance company, and certain kinds of partnerships. (See articles 801–2 and 801–4.) The definitions, terms, and classifications, as set forth in section 801, shall have the same respective meaning and scope in these regulations.

ART. 801–2. *Association.*—The term "association" is not used in the Act in any narrow or technical sense. It includes any organization, created for the transaction of designated affairs, or the attainment of some object, which, like a corporation, continues notwithstanding that its members or participants change, and the affairs of which, like corporate affairs, are conducted by a single

individual, a committee, a board, or some other group, acting in a representative capacity. It is immaterial whether such organization is created by an agreement, a declaration of trust, a statute, or otherwise. It includes a voluntary association, a joint-stock association or company, a "business" trust, a "Massachusetts" trust, a "common law" trust, an "investment" trust (whether of the fixed or the management type), an interinsurance exchange operating through an attorney in fact, a partnership association, and any other type of organization (by whatever name known) which is not, within the meaning of the Act, a trust or an estate, or a partnership. If the conduct of the affairs of a corporation continues after the expiration of its charter, or the termination of its existence, it becomes an association.

ART. 801–3. *Association distinguished from trust.*—The term "trust," as used in the Act, refers to an ordinary trust, namely, one created by will or by declaration of the trustees or the grantor, the trustees of which take title to the property for the purpose of protecting or conserving it as customarily required under the ordinary rules applied in chancery and probate courts. The beneficiaries of such a trust generally do no more than accept the benefits thereof and are not the voluntary planners or creators of the trust arrangement. Even though the beneficiaries do create such a trust, it is ordinarily done to conserve the trust property without undertaking any activity not strictly necessary to the attainment of that object.

As distinguished from the ordinary trust described in the preceding paragraph is an arrangement whereby the legal title to the property is conveyed to trustees (or a trustee) who, under a declaration or agreement

of trust, hold and manage the property with a view to income or profit for the benefit of beneficiaries. Such an arrangement is designed (whether expressly or otherwise) to afford a medium whereby an income or profit-seeking activity may be carried on through a substitute for an organization such as a voluntary association or a joint-stock company or a corporation, thus obtaining the advantages of those forms of organization without their disadvantages.

If a trust is an undertaking or arrangement conducted for income or profit, the capital or property of the trust being supplied by the beneficiaries, and if the trustees or other designated persons are, in effect, the managers of the undertaking or arrangement, whether the beneficiaries do or do not appoint or control them, the beneficiaries are to be treated as voluntarily joining or cooperating with each other in the trust, just as do members of an association, and the undertaking or arrangement is deemed to be an association classified by the Act as a corporation.

By means of such a trust the disadvantages of an ordinary partnership are avoided, and the trust form affords the advantages of unity of management and continuity of existence which are characteristic of both associations and corporations. This trust form also affords the advantages of capacity, as a unit, to acquire, hold, and dispose of property and the ability to sue and be sued by strangers or members, which are characteristic of a corporation; and also frequently affords the limitation of liability and other advantages characteristic of a corporation. These advantages which the trust form provides are frequently referred to as resemblance to the general form, mode

of procedure, or effectiveness in action, of an association or a corporation, or as "quasi-corporate form." The effectiveness in action in the case of a trust or of a corporation does not depend upon technical arrangements or devices such as the appointment or election of a president, secretary, treasurer, or other "officer," the use of a "seal," the issuance of certificates to the beneficiaries, the holding of meetings by managers or beneficiaries, the use of a "charter" or "by-laws," the existence of "control" by the beneficiaries over the affairs of the organization, or upon other minor elements. They serve to emphasize the fact that an organization possessing them should be treated as a corporation, but they are not essential to such classification, for the fundamental benefits enjoyed by a corporation, as outlined above, are attained, in the case of a trust, by the use of the trust form *itself*. The Act disregards the technical distinction between a trust agreement (or declaration) and ordinary articles of association or a corporate charter, and all other differences of detail. It treats such a trust according to its essential nature, namely, as an association. This is true whether the beneficiaries form the trust or, by purchase or otherwise, acquire an interest in an existing trust.

The mere size or amount of capital invested in the trust is of no importance. Sometimes the activity of the trust is a small venture or enterprise, such as the division and sale of a parcel of land, the erection of a building, or the care and rental of an office building or apartment house; sometimes the activity is a trade or business on a much larger scale. The distinction is that between the activity or purpose for which an ordi-

nary strict trust of the traditional type would be created, and the activity or purpose for which a corporation for profit might have been formed.

ART. 801–4. *Partnerships.*—The Act provides its own concept of a partnership. Under the term "partnership" it includes not only a partnership as known at common law but, as well, a syndicate, group, pool, joint venture, or other unincorporated organization which carries on any business, financial operation, or venture, and which is not, within the meaning of the Act, a trust, estate, or a corporation. On the other hand the Act classifies under the term "corporation" an association or joint-stock company, the members of which may be subject to the personal liability of partners. If an organization is not interrupted by the death of a member or by a change in ownership of a participating interest during the agreed period of its existence, and its management is centralized in one or more persons in their representative capacities, such an organization is an association, taxable as a corporation. As to the characteristics of an association, see also articles 801–2 and 801–3. The following examples will illustrate some phases of these distinctions:

(1) If A and B buy some acreage for the purpose of subdivision, they are joint adventurers, and the joint venture is classified by the Act as a partnership.

(2) A, B, and C each contributes $10,000 for the purpose of buying and selling real estate. If A, B, C, or D, an outside party (or any combination of them as long as the approval of each participant is not required for syndicate action), takes control of the money, property and business of the enter-

prise, and the syndicate is not terminated on the death of any of the participants, the syndicate is classified as an association.

ART. 801–5. *Limited partnership as corporation.*—Limited partnerships of the type of partnerships with limited liability or partnership associations authorized by the statutes of Pennsylvania and a few other States are only nominally partnerships. Such so-called limited partnerships, offering opportunity for limiting the liability of all the members, providing for the transferability of partnership shares, or having other material characteristics of corporate form, must make returns of income and pay the tax as corporations. In all doubtful cases limited partnerships will be treated as corporations unless they submit satisfactory proof that they are not in effect so organized. A Michigan partnership association is taxable as a corporation.

U. S. GOVERNMENT PRINTING OFFICE: 1940

In the

SUPREME COURT OF THE UNITED STATES

October Term, 1940

No. 184

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, *Petitioner,*

VS.

HORSESHOE LEASE SYNDICATE, *Respondent.*

On Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Fifth Circuit

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BRIEF FOR RESPONDENT IN OPPOSITION TO THE PETITION FOR WRIT OF CERTIORARI

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INDEX TO SUBJECT MATTER

Page

Introduction 1

Opinion Below 2

Jurisdiction 2

Question Presented 2

Statutes and Regulations Involved 3

Statement 3

Summary of Argument 5

I. The decision is correct.

II. The decision below does not conflict with any decision in any other circuit and it does not conflict with any decision of this Court.

III. The question presented requires the application of principles, fixed by decisions, to the peculiar facts in each case which is under consideration.

Argument 5

Point I 5

Point II 19

Point III 25

Conclusion 35

INDEX TO AUTHORITIES CITED

Page

Baldwin's Century Ed. of Bouvier's Law Dictionary 15

Bert v. Helvering, 92 F. (2d) 491 (App. D. C.) 24, 29

Burk-Waggoner Oil Association v. Hopkins, 269 U. S. 110, affirming District Court 296 F. 492 .....23, 24

Commissioner v. Fleming, 82 F. (2d) 324, (C. C. A. 5th) 14, 19

Commissioner v. Highlands E. L. Subd., etc. 88 F. (2d) 355 (C. C. A. 7th), certiorari denied 302 U. S. 691 .....26, 31

Commissioner v. N. B. Whitcomb Coca-Cola Syndicate, 95 F. (2d) 596, (C. C. A. 5th) aff'g 35 B. T. A. 1031 .....15, 23, 29

Commissioner v. Vandegrift Realty Co., 82 F. (2d) 387 (C. C. A. 9th) 25, 30

Crabb v. Bell (Tex. Civ. App.) 220 S. W. 623 .....14, 19

Everts, C. A., et al. v. Commissioner, 38 B. T. A. 1039 21

Hecht v. Malley et al., former Collector of Internal Revenue, 44 S. Ct. 462, 265 U. S. 144 5

Helvering v. Coleman-Gilbert Associates, 296, U. S. 369, 56 S. Ct. 285 ..... 8, 12

Page

Helvering v. Combs, 296 U. S. 365, 56 S. Ct. 287....8, 26, 31

Lewis, A. A. & Company et al. v. Comm., 57 S. Ct. 799, 301 U. S. 385 ....16, 19, 28

McEntire v. Thomasson (Tex. Civ. App.) 210 S. W. 563 ....14, 19

Monrovia Oil Co. v. Commissioner, 83 F. (2d) 417, (C. C. A. 9th) 24

Morrissey v. Commissioner, 56 S. Ct. 289, 296 U. S. 344 ....6, 8, 16, 26, 28, 31, 35

Swanson v. Commissioner, 56 S. Ct. 283, 296 U. S. 362 8

Thrash Lease Trust v. Commissioner, 36 B. T. A. 444, 99 F. (2d) 925 (C. C. A. 9th), certiorari denied, 306 U. S. 654 ....20, 21, 22

Title Insurance & Trust Co. v. Commissioner, 100 F. (2d) 482 (C. C. A. 9th) 24

United States v. Trust No. B. I. 35, 107 F. (2d) 22 (C. C. A. 9th) 26, 31

Wellston Hill Syndicate Fund v. Commissioner, 101 F. (2d) 924 (C. C. A. 8th) 24

Wholesalers Adjustment Co. v. Commissioner, 88 F. (2d) 156 (C. C. A. 8th) 24

STATUTES AND REGULATIONS INVOLVED

Page

Judicial Code:

Sec. 240 (a) 2

Revenue Act of 1932:

Sec. 13 36
Sec. 52 36
Sec. 181 37
Sec. 182 37
Sec 189 37
Sec. 1111 ..... 2, 36

Revised Civil Statutes of Texas:

Art. 5924 40

Treasury Regulations 77:

Art. 1311 38
Art. 1312 38
Art. 1313 38
Art. 1314 39
Art. 1320 39

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BRIEF FOR RESPONDENT IN OPPOSITION TO THE PETITION FOR WRIT OF CERTIORARI

INTRODUCTION

On June 26, 1940, petition was filed on behalf of petitioner, praying that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Fifth Circuit entered in the above entitled cause on March 26, 1940.

The respondent opposes the petition for writ of certiorari for the reasons hereinafter set out.

OPINIONS BELOW

The unpublished Memorandum Opinion of the United States Board of Tax Appeals is printed in the record at pages 13 to 24, inclusive.

The decision of the United States Board of Tax Appeals is printed in the record at page 25.

The Opinion of the United States Circuit Court of Appeals is reported in 110 F. (2d) 748.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on March 26, 1940, and the jurisdiction of this Court has been invoked under *Section 240 (a) of the Judicial Code* as amended by the *Act of February 13, 1925.*

Notice of filing the petition herein, together with notice that no brief in support will be filed, copies of petition and transcript of record were served on counsel for respondent on July 12, 1940.

QUESTION PRESENTED

The question presented is as follows:

For the calendar year 1932, was respondent an associate within the meaning of Section 1111 (a) (2) of

the Revenue Act of 1932 and as such subject to income tax as a corporation?

STATUTES AND REGULATIONS INVOLVED

The pertinent provisions of the statutes and regulations involved are set forth in the Appendix, *infra*, pages 36-40.

Articles 801-1 to 801-5 of Regulations 86 promulgated under the Revenue Act of 1934 set forth on pages 22 to 27 of the petition have no application here.

STATEMENT

The statement set out on pages 2 to 13, inclusive, of the petition herein is substantially correct.

The Court below has correctly and succinctly set out the important facts.

In 1931, the several owners of a tract of land in Texas executed a mineral lease thereon to J. Edgar Finley, P. T. Fullwood and the Patterson Drilling Company, a corporation, pursuant to an agreement between said parties, under the terms of which the lessees were required to organize a syndicate having 350 units of a par value of $100 each, to sell the units, and, from the proceeds, to drill an oil well on the property. The consideration to the lessors was a 1/8 royalty, a yearly rental of $1 per acre, and 35 units.

Finley, Fullwood, and the Patterson Drilling Company assumed the name Horseshoe Lease Syndicate, di-

vided their joint interest in the lease into 350 fractional parts, and sold as many of said parts as they desired, delivering to the purchasers an assignment of one or more fractional parts in accordance with their purchase. Under the provisions of the assignment, the assignors contracted to drill a well with their equipment, and to operate, market, manage, and account for all proceeds thereof. Each purchaser executed in favor of the assignors a power of attorney, empowering them to act for and in behalf of all co-owners in all matters relating to the property of the syndicate, thereby vesting the management and control in the three attorneys in fact. No provision was made for the perpetuation of the management so created, or for the succession or substitution of attorneys in fact. The fractional parts purchased by assignment were readily transferable by reassignment, and many such transfers were made. The well contracted to be drilled by the assignors was to be paid for by them, and any additional wells drilled were to be paid for out of the proceeds of the wells then producing. Excepting this stipulation, there was no other limitation of liability in favor of the assignees. The net earnings of the enterprise periodically were to be computed and divided among the co-owners as their interests appeared; no surplus was to be created, and no salaries were to be paid.

Organized and operating in this manner, the first well was drilled successfully, and, sometime later, another producing well was drilled from the proceeds of the first. The net income derived therefrom was paid

to the co-owners in accordance with the agreement, and was reported by them in their individual income tax returns. The syndicate filed a partnership return for the year 1932, and the Commissioner claimed that a corporation return should have been filed, thereby creating the issue here. (R. 168-169)

SUMMARY OF ARGUMENT

I.

The decision below is correct.

II.

The decision below does not conflict with any decision in any other circuit and it does not conflict with any decision of this Court.

III.

The question presented requires the application of principles, fixed by decisions, to the peculiar facts in each case which is under consideration.

ARGUMENT

I.

The decision below is correct.

In the case of *Hecht v. Malley et al., former Collector of Internal Revenue* and associated cases, *44 S. Ct. 462, 265 U. S. 144,* this Court said among other things:

"The word 'association' appears to be used in the Act in its ordinary meaning. It has been defined as a term 'used throughout the United States to signify *a body of persons united without a charter, but upon the methods and forms used by incorporated bodies for the prosecution of some common enterprise.*'" (Italics supplied)

In the more recent case of *Morrissey v. Commissioner, 56 S. Ct., 289, 296 U. S. 344*, decided under the Revenue Acts of 1924 and 1926, this Court said in part as follows:

"'Association' implies associates. It implies the entering into a joint enterprise, and, as the applicable regulation imports, an enterprise for the transaction of business. This is not the characteristic of an ordinary trust — whether created by will, deed or declaration — by which particular property is conveyed to a trustee or is to be held by the settlor, on specified trusts, for the benefit of named or described persons. Such beneficiaries do not ordinarily, and as mere cestuis que trust, plan a common effort or enter into a combination for the conduct of a business enterprise * * *. As we have seen the classificiation cannot be said to require organization under the statute, or with statutory privileges. The term embraces associations as they may exist at common law. *Hecht v. Malley, supra.* We have already referred to the definitions, quoted in that case, showing the ordinary meaning of the term as applicable to a body of persons united without a charter 'but upon the methods and forms used by incorporated bodies for the prosecution of some common enterprise.' * * *

"What, then, are the salient features of a trust —when created and maintained as a medium for the carrying on of a business enterprise and sharing its gains—which may be regarded as making it analogous to a corporate organization? *A corporation, as an entity, holds the title to the property embarked in the corporate undertaking. Trustees, as a continuing body with provision for succession, may afford a corresponding advantage during the existence of the trust.* Corporate organization furnishes the opportunity for a centralized management through representatives of the members of the corporation. The designation of trustees, who are charged with the conduct of an enterprise, who act *'in much the same manner as directors', may provide a similar scheme, with corresponding effectiveness.* Whether the trustees are named in the trust instrument with power to select successors, so as to constitute a self-perpetuating body, or are selected by, or with the advice, of those beneficially interested in the undertaking, centralization of management analogous to that of corporate activities may be achieved. An enterprise carried on by means of a trust may be secure from termination or interruption by the death of owners of beneficial interests and in this respect their interests are distinguished from those of partners and are akin to the interests of members of a corporation. And the trust type of organization facilitates, as does corporate organization, the transfer of beneficial interests without affecting the continuity of the enterprise, and also the introduction of large numbers of participants. The trust method also permits the limitation of the personal liability of participants to the property embarked in the undertaking.

"It is no answer to say that these advantages flow from the very nature of trusts. For the question has arisen because of the use and adaption of the trust mechanism. The suggestion ignores the postulate that we are considering those trusts which have the distinctive feature of being created to enable the participants to carry on a business and divide the gains which accrue from their common undertaking, trusts that thus satisfy the primary conception of association and have the attributes to which we have referred, distinguishing them from partenerships. *In such a case, we think that these attributes make the trust sufficiently analogous to corporate organization to justify the conclusion that Congress intended that the income of the enterprise should be taxed in the same manner as that of corporations.*" (Italics supplied)

On the same day that the Morrissey case was decided this Court decided the following cases involving the same question with which we are here concerned:

Swanson v. Commissioner, 56, S. Ct. 283, 296 U. S. 362;

Helvering v. Combs, 296 U. S. 365, 56 S. Ct. 287;

Helvering v. Coleman-Gilbert Associates, 296 U. S. 369, 56 S. Ct. 285.

The important facts in connection with this question in the four cases cited, supra, are summarized below.

In the *Morrissey* case, supra, the petitioner, in 1921, made a declaration of trust of real estate in Los Angeles, designating the enterprise as Western Avenue Golf Club.

(1) The trustees were authorized to add to their number and choose successors, to purchase, encumber, sell, lease and operate the described or other lands and to construct and operate golf courses, etc.

(2) The trustees were authorized to receive rents, profits and income and to make loans and investments.

(3) The trustees were authorized to make regulations and to generally manage the trust estate as if the trustees were its absolute owners.

(4) The trustees were declared to be without power to bind the beneficiaries personally, those dealing having only the right to look to the property for satisfaction.

(5) The beneficial interests were evidenced *solely by transferable certificates* for shares, 2000 preferred, $100 par, and 2000 common, no par.

(6) Trustees were empowered to call meetings of shareholders, but votes of the shareholders were to be advisory only.

(7) *It was provided that the death of a trustee was not to end the trust*, which was to continue for 25 years unless terminated sooner by the trustees.

(8) Beneficial interests were sold, but *title to the real estate remained in the trustees.*

In the *Swanson* case, supra, the following important facts existed:

(1) One Swanson and one Otis acquired vacant land with the view of improving it by erecting an apartment house and a trust agreement was formed for the purpose of carrying *title* to the property, the first trustees being Otis, Swanson and Mills. The trust was designated "Lake View Land Association."

(2) The trustees were given complete management and control of the property, power to exchange, reconstruct, remodel, sell or improve the property; to borrow money secured by the property; to rent suitable quarters to transact the trust business and employ assistants; to issue receipts evidencing interests of beneficiaries, representing *1000 shares of the par value* of $100 each.

(3) It was provided that the receipts were evidences of ownership of *personal property* and not real estate.

(4) It was provided that the certificates could be *transferred by assignment.*

(5) The agreement provided that the *trust could sue and be sued.*

(6) It was provided that the *trustees were not personally liable* and that persons dealing would look only to the property.

(7) It was provided that the trust should terminate at the end of 20 years after the death of the last survivor of certain persons, or by disposing of all the property.

(8) *It was provided that the trust had succession and was not terminated by death.*

(9) It was provided that the compensation of the trustees was to be fixed by themselves but not to exceed 2½% of the gross income.

(10) It was provided that after making provision for the payment of outstanding claims, the net income was to be divided among the beneficiaries according to their interests.

In the *Combs case*, supra, the following important facts existed:

(1) A trust was created to finance and drill a well for the production and sale of oil. Under a trust agreement, the Hub Oil Company, owner of the lease, assigned it to E. E. Combs and Edward Everett as trustees.

(2) The agreement described as beneficiaries all persons who may own or acquire a portion of the whole beneficial interest as defined, the whole beneficial interest being defined as 71 plus per cent of gross production, and the beneficiaries were to be paid their pro rata share after the deduction for payment of trust obligations, i. e., 25% to beneficiaries who provided the money and 44 plus per cent to E. E. Combs and 2% to Edward Everett.

(3) The trust provided for the certificates of beneficial interests to be issued in approved legal form.

(4) Thirteen persons were named as beneficiaries with amounts contributed and the percentages owned by each, these amounts aggregating $25,000.

(5) *The certificate of beneficial interest recited that the party named was the holder of the beneficial interest transferable upon the books of the trustee upon endorsement and surrender of the certificates.*

(6) *The trustees were authorized to hold title to all property and property rights, the legal title to which might vest in them under the trust, to use the moneys deposited by the beneficiaries, to pay labor, to pay debts, to borrow money upon credit of the trust and to sell any unsold beneficial interests etc.*

(7) *The trustees were not to be individually liable except for willful misconduct.*

(8) *All proceeds of sale were to be placed in a designated bank.*

In the *Coleman-Gilbert Associates* case, supra, the following important facts existed:

(1) Five individuals, being the co-owners of twenty apartment houses in Boston, formed by indenture the Coleman-Gilbert Associates.

(2) By the trust instrument, which recited a contemporaneous conveyance of the property to themselves, they declared that the real estate so conveyed and any real estate thereafter acquired under the trust should be held by them *in trust* for the purposes described with the designation "Coleman-Gilbert Associates."

(3) The trust was to continue for 15 years unless sooner terminated by sale or disposition of the estate.

(4) The trustees were to hold title to the property in order to improve and dispose of it for the benefit of persons named as "cestuis que trustent and beneficiaries, and their respective representatives and assigns, devisees, or legatees" in the shares provided in the instrument.

(5) It was provided that the beneficiaries were to have no interest in the trust property and especially were they to have no right to call for any partition thereof.

(6) *It was provided that the interests of the beneficiaries were to be personal property.*

(7) *It was provided that the death of any one or of all the beneficiaries was not to determine the trust nor entitle the legal representatives of the decedent to an accounting by the trustees.*

(8) It was provided that the trustees had full power and discretion as absolute owners, being authorized to invest and reinvest the trust property, including income, in mortgages and and other obligations secured upon real estate and in the purchase and improvement of real estate situated in the cities and towns of the commonwealth of Massachusetts.

(9) The trustees were authorized to sell at public or private sale all or any part of the property; to hire

for improvement or otherwise, lease, exchange, release, borrow money and to make contracts.

(10) It was provided that funds in possession of the trustees not required in the judgment of the trustees for development and improvements were to be divided and paid over annually or oftener, *if convenient*, to the beneficiaries.

(11) *It was provided that the trustees were to have no power to bind the beneficiaries personally.*

(12) *Provision was made for resignation of the trustees and for the apponitment by the surviving trustees of successors but if the surviving trustees failed to do this, the beneficiaries had the right of selecting successor trustees.*

(a) In the case under consideration the owners of undivided fractional intrests in the lease were not associated or united upon the methods or forms used by incorporated bodies for the prosecution of a common enterprise.

(b) The undivided fractional interests in the oil and gas lease which the lessees owned were interests in real estate which the owners held as tentants in common under the laws of Texas.[1]

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1. Comm. v. Fleming, 82 F. (2d) 324, (C. C. A. 5th); Crabb v. Bell (Tex. Civ. App.) 220 S. W. 623; McEntire v. Thomasson (Tex. Civ. App.) 210 S. W. 563.

(c) Shares of stock in a corporation are now universally considered to be personal property.[1]

(d) Each purchaser of an undivided fractional interest in the lease gave to the sellers a written power of attorney and, therefore, each joint owner in legal effect was active in connection with the operation of the lease. *Qui facit per alium, facit per se.* It is clear that activities under written and separate power of attorney from each owner of an interest in a lease is not similar to Corporate activities.[2]

(e) There was no limited liability except the provision in the contract with the fee owners who gave the lease that the 35/350 given to them as part consideration for the lease would not be assessed for drilling or operating costs.

(f) There was no trust agreement of any kind and the co-owners or joint tenants derived no benefits enjoyed by associates, stockholders or beneficiaries of a trust through the manner and method in which their property was operated.

(g) No trustee or trustees and no entity of any kind held title, equitable or legal, to any interest in the lease for the benefit of any other person. Each owned his in-

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1. Baldwin's Century Edition of Bouvier's Law Dictionary.

2. Comm. v. N. B. Whitcomb Coca-Cola Syndicate, 95 F. (2d) 596 (C. C. A. 5th) affg 35 B. T. A. 1031.

terest in the lease, in real property under the laws of Texas, and there was no entity of any kind separate and distinct from the co-owners. In *Morrissey v. Commissioner*, supra, this Court said among other things:

> "A corporation as an entity holds the title to the property embarked in the corporate undertaking. Trustees, as a continuing body, with provision for succession may afford a corresponding advantage during the existence of the trust."

(h) The consideration paid by each purchaser of interest in the lease was paid to and belonged to the sellers. It was not the property of any entity. It cannot be compared with capital of a corporation.

(i) No provision was made for succession.

(j) No provision was made that the interests which the co-owners had in the lease should be personal property.

(k) No provision was made for majority control.

(l) No corporate formalities were ever observed.

The characteristics of the syndicate are not in any degree analogous to the characteristics of an ordinary corporation.

It is insisted that the facts in the four Supreme Court cases relied on by petitioner are not at all similar to the facts in the case under consideration and that the facts in this case are more analogous to the facts in the case of *A. A. Lewis & Company et al. v. Commissioner, 57 S. Ct. 799, 301 U. S. 385*, decided by this Court in

which it was held that there was no association and no corporation income tax liability. In this case it was said among other things:

> "If it were not for the declaration of trust, we should have here the simple case of an appointment by a land owner of an agent to subdivide the land and sell it, receiving as compensation for his services a fixed percentage of the payments made by the purchasers. *It is quite evident that such an arrangement has no element of substance or method which would warrant its designation as an association under the statutory provision in question.* (Revenue Act of 1928) *Nor can we see that the intervention of a trustee to hold title, execute contracts and conveyances at the direction of the real-estate agent and make collections alters the situation.*
>
> "The question recently has received full consideration in Morrissey v. Commissioner, 296 U. S. 344, and three other cases which immediately follow in the same volume. The trust reviewed in the Morrissey case was essentially unlike that now under consideration. There the trust was a medium for the carrying on of a business enterprise by the trustees and participation in the profits by numerous *beneficiaries whose interests were represented by transferable share certificates, thus permitting the introduction of new participants without affecting the continuity of the plan. The certificates represented both perferred and common shares.* We pointed out that the corporate analogy was evidenced by centralized control, continuity and limited liability, as well as by the issue of transferable certificates; and we said (page 356) that the word 'association' implies associates. 'It implies the entering into a joint enterprise, and, as the applicable

(departmental) regulation imports, an enterprise for the transaction of business. This is not the characteristic of an ordinary trust—whether created by will, deed, or declaration—by which particular property is conveyed to a trustee or is to be held by the settlor, on specified trusts, for the benefit of named or described persons. Such beneficiaries do not ordinarily, and as mere cestuis que trustent, plan a common effort or enter into a combination for the conduct of a business enterprise.'

"The arrangement here answers the foregoing description of an ordinary trust—that is, it was created in virtue of a declaration by which a designated piece of real property was conveyed to the trustee on specified trusts, for the benefit of definitely named persons, one of whom was the grantor of the land and the other an agent of the grantor for the sole purpose of subdividing and selling the land. The agent was designated by name, and his powers definitely fixed in advance of their exercise. *He possessed no authority beyond that expressly delegated by his principal.* The trust was adopted merely as a convenient means of making effective the sales of the agent under the contract. The duties of the trustee were purely ministerial, with no power to control, direct, or participate in, the conduct of the selling enterprise contemplated by the contract. There is to be found in the operation of the business no essential characteristic of corporate control—nothing analogous to a board of directors or shareholders, no exemption from personal liability, no issue of transferable certificates of interest. *There is simply the common relation of principal and agent, coupled with the collateral incidents of an ordinary trust. We are not able to find in the situation an 'association' within the meaning of*

the statute under consideration, because there are no associates and no feature 'making (the trust) analogous to a corporate organization.'" (Italics supplied)

Here, as in the *Lewis* case, we have the relationship of principal and agent, Finley, Fullwood and Patterson Drilling Company being the agents and each purchaser of undivided fractional interest in the lease being principal. There was no organization because each owner of an interest in the lease was acting in connection with the drilling and operation of the lease through the agents authorized in power of attorney (R. 168). *Qui facit per alium facit per se. The legal title to the property was not separated from the beneficial ownership. There was no entity of any kind and no trustee holding title for anyone else.* Each owned his own interest in the property which was an interest in real estate under the laws of Texas.[1]

It is urged that clearly the decision that Horseshoe Lease Syndicate was not an association is correct.

II.

The decision below does not conflict with any decision in any other circuit and it does not conflict with any decision of this Court.

On page 14 of the petition herein among other things the following statement is made:

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1. Commissioner v. Fleming, 82 F. (2d) 324, (C. C. A. 5th); Crabb v. Bell, 220 S. W. 623 (Texas); McEntire v. Thomasson, 210 S. W. 563.

"The decision below is in substantial conflict with *Thrash Lease Trust v. Commissioner*, 99 F. (2d) 925 (C. C. A. 9th), certiorari denied, 306 U. S. 654. There an arrangement similar to the arrangement in the instant case was entered into for the development and exploitation of an oil and gas lease in Texas. The lease was assigned to one Gordon MacMillan, as trustee, and the development of the property and assignment of the interests were carried out in much the same manner as those details were carried out in the instant case. Percentage interests were assigned to many persons, some of the interests purporting to be interests in the oil and gas and some purporting to be interests in the lease."

In the *Thrash Lease Trust* case (36 B. T. A. 444)[1] it was held by the United States Board of Tax Appeals that

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1. In the *Thrash Lease Trust case*, the Board of Tax Appeals among other things said:

"Although, from the evidence, the organization is amorphous indeed, there is little doubt that there was an organization of individuals holding transferable shares in a common business enterprise managed by one or two of their number, who distributed the profits proportionately with interest. This is enough to give prima facie substance to the Commissioner's treatment of it as an association, Morrissey v. Commissioner, 296 U. S. 344; Helvering v. Combs 296 U. S. 365; Helvering v. Coleman-Gilbert Associates, 296 U. S. 369; Swanson v. Commissioner, 296 U. S. 362; Bert v. Helvering, 92 Fed. (2d) 491, and to require an affirmative showing by the petitioner of attributes and circumstances indicating a different taxable character under the revenue statute. No such showing is in this record, and the determination must stand."

the Thrash Lease Trust was an association. The Board of Tax Appeals in the *Thrash Lease Trust* case held that the facts were not sufficient to overcome the showing made in favor of the Commissioner's determination.[1]

In addition to the fact that in the *Thrash Lease Trust* case the Board of Tax Appeals based its opinion in part on the fact that the Thrash Lease Trust had not overcome the burden placed on it, the United States Circuit Court of Appeals for the Ninth Circuit in affirming the Board of Tax Appeals commented significantly on the

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1. In the case of *C. A. Everets et al. v. Commissioner of Internal Revenue, 38 B. T. A. 1039*, the Board of Tax Appeals commented on the decision in the *Thrash Lease Trust* case as follows:

   "In Thrash Lease Trust, 36 B. T. A. 444, cited by respondent, we did not think that the facts were sufficient to overcome the showing made in favor of the correctness of the Commissioner's determination and in that respect is distinguished from the instant case."

fact that title to the property was in part in a trustee.[1] This is one of the most important considerations.

It is thus seen that in the *Thrash Lease Trust* case emphasis was placed by the Circuit Court upon the fact that a trustee held title for the benefit of others; that there was a trust, an entity which was operated like a corporation, and that there was sufficient analogy to a corporate organization to justify the action of the Commissioner in determining that the income involved should be taxed in the same manner as that of a corporation. The *Thrash Lease Trust* case, therefore, is quite different on its facts from the case under consideration.

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1. In the case of *Thrash Lease Trust v. Commissioner, 99 F. (2d) 925, Certiorari denied, 306 U. S. 654*, the Ninth Circuit said among other things as follows:

   "This was not any ordinary trust. *The title to the property, as far as the percentage shareholders were concerned, was in a single person denominated trustee. The respective interests of the several percentage holders were subject to transfer*; the management, so far as appears, was centered in the MacMillans, who conducted the business much after the manner of directors of a corporation.

   "This is a border line case. *The entity* here, the Thrash Lease Trust, petitioner, in its general structure and method of operation, is sufficiently *analogous to a corporate organization to justify the action of the Commissioner in determining that the income of the enterprise should be taxed in the same manner as that of a corporation.*" (Italics supplied)

Here, we have no entity separate and apart from the individual owners. Each owns an interest in real estate and each person owning an interest acted either personally or through his agents and attorneys in fact, similar in substantial respects to the case of *Commissioner v. N. B. Whitcomb Coca-Cola Syndicate, 95 F. (2d) 596, affirming 35 B. T. A. 1031.*[1]

It is contended in the petition that the decision below conflicts also with the case of *Burk-Waggoner Oil Association v. Hopkins, 269 U. S. 110, affirming District Court 296 Fed. 492.* The facts in the Burk-Waggoner Oil Association case have no reasonable resemblence to the facts in this case. And there is no conflict between

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1. In the Whitcomb Coca-Cola case, the Fifth Circuit said among other things as follows:

> "There was no trust in a technical sense, for the manager was not to hold title to any property for the use of others. Each share bought was to be participated in by each subscriber in proportion to his interest in the Syndicate. Each share was thus owned by the subscribers in common. The manager was not the agent of an aggregation of subscribers, that is to say, of an entity, but the authority was expressly to buy and sell the stock 'for the account of each subscriber.'"

the decision in the instant case and the decision of this Court in the Burk-Waggoner Oil Association case.[1]

In the petition, (p. 17), it is insisted that the decision below is in conflict with the following cases to the extent that it fails to apply the principles established by the Supreme Court decisions:

Monrovia Oil Co. v. Commissioner, 83 F. (2d) 417 (C. C. A. 9th);

Wholesalers Adjustment Co. v. Commissioner, 88 F. (2d) 156, (C. C. A. 8th);

Bert v. Helvering, 92 F. (2d) 491 (App. D. C.);

Title Insurance & Trust Co. v. Commissioner, 100 F. (2d) 482 (C. C. A. 9th);

Wellston Hills Syndicate Fund v. Commissioner, 101 F. (2d) 924, (C. C. A. 8th).

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1. In the *Burk-Waggoner Oil Association* case, this Court held that that Association was liable to tax as a corporation. There was a joint stock association in that case operating under a trust agreement. It was to continue for twenty-one years after the death of the last of six trustees. The purpose of the joint stock association was to purchase or lease oil lands and to develop and operate them. There was capital stock of $60,000 divided into 600 shares of par value of $100 each. Provision was made for transfer of certificates and corporate formalities were observed except that no corporate charter was filed.

In each of these cases it is clear that, unlike the facts in this case, the legal title to the assets was separated from the beneficial ownership and that many formalities of a corporation were observed.

In view of the above, it is insisted that the decision herein is not in conflict with any decision of any circuit or with any decision of this Court.

III.

The question presented requires the application of principles, fixed by decisions, to the peculiar facts in each case which is under consideration.

In the petition (p. 17) under "Reasons for Granting the Writ," the following statement is made:

> "Whether the Horseshoe Lease Syndicate is an association within the statutory definition was treated by the court below as a question of fact, and it limited its review simply to an examination of whether there was 'substantial evidence to support' what it described as 'the finding' of the Board of Tax Appeals. In so limiting the scope of review, the decision below is in direct conflict with a number of decisions which treat the question as one of law, and in each one of which the judgment of the lower tribunal was reversed."

The following cases are then cited:

Commissioner v. Vandegrift Realty Co., 82 F. (2d) 387 (C. C. A. 9th);

Commissioner v. Highlands E. L. Subd., etc., 88 F. (2d) 355 (C. C. A. 7th), *certiorari denied*, 302 U. S. 691;

United States v. Trust No. B. I. 35, 107 F. (2d) 22 (C. C. A. 9th);

Helvering v. Combs, 296 U. S. 365.

It is insisted that the decision below follows the principles laid down in the case of *Morrissey v. Commissioner*, supra, and other cases decided by this Court. In each of the above cited cases the legal title to the property involved was separated from the beneficial ownership; there was an origanization engaged in business and corporate formalities were observed.

In the decision below herein the Court in following the case of *Morrissey v. Commissioner*, supra, said in part as follows:

> "It has been said that no inelastic rule can be advanced to settle the question, due to the variety of circumstances under which it may arise, but that the facts of each case must control its determination." Citing *Morrissey v. Commissioner.*

The language of the Court below to which exception is taken in this connection is perhaps in the following sentences:

> "The determination of this issue depends upon whether the syndicate, so organized and operated,

resembles a corporation more nearly than it does a partenership, not being either exactly. Commissioner v. Brouillard, 70 F. (2) 154; Bert v. Helvering, 92 F. (2) 491. This is a question of fact, and the Board of Tax Appeals, under the stipulated facts, found that, for purposes of the income tax laws, the syndicate more nearly resembled a partnership. This finding must be upheld by this court if there is substantial evidence to support it, even though conflicting inferences fairly might be drawn by reasonable men from the undisputed facts. South Chicago Coal & Dock Co. v. Bassett, — U. S. — (Feb. 26, 1940) . . . From the undisputed facts above stated, a reasonable inference of fact may fairly be drawn that respondent was not an association within the meaning of the statute. Therefore, there is substantial evidence to support the finding of the board to this effect, and its conclusion of law that respondent was not subject to income tax as a corporation was correct." (R. 169)

It is thus seen that the lower Court held that the determination of this issue (the association issue) depended upon whether the syndicate resembled a corporation more nearly than it did a partnership and that this (the question of resemblance or analogy) was a question of fact. It is clear that the lower Court in so ruling herein was following the principles fixed by this Court in the four leading cases cited above.

In the *Morrissey* case, supra, this Court said among other thing:

> "In such a case, we think that those attributes make the trust sufficiently analogous to corporate

> organization to justify the conclusion that Congress intended that the income of the enterprise should be taxed in the same manner as that of corporations."

Again, this Court said in the case of *A. A. Lewis & Company et al. v. Commissioner*, supra:

> "We pointed out that the corporate analogy was evidenced by centralized control, continuity and limited liability, as well as by the issue of transferable certificates; and we said that the word 'association' implies associates."

It is insisted that it is clear that this Court in these two cases and other cases has laid down the rule that in deciding this question it is necessary that the attributes (or characteristics) of the alleged association be compared with those of corporate organization to determine their analogy (or resemblance) to a corporate organization. It is clearly necessary that the facts in each particular case be carefully considered and that facts in each case shall govern in the decision on this question and that is the way the United States Court of Appeals for the District of Columbia in the

case of *Bert v. Helvering*, 92 F. (2d) 491,[1] and the United States Circuit Court of Appeals for the Fifth Circuit in the case of *N. B. Whitcomb Coca-Cola Syndicate*, 95 F. (2d) 596, *affirming* 35 B. T. A. 1031,[2] have each so construed the principles laid down by this Court.

The Court below has considered the peculiar facts in the case as have other courts which have followed the principles laid down by decisions of this Court and it is clear that, in any and all cases involving this question, it is absolutely necessary that each case be given

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1. In the *Bert* case, the United States Court of Appeals for the District of Columbia said in part as follows:

   "And, as we have seen, the Supreme Court has expressly abolished the control test as a factor in applying the provision of the income tax law applicable here, but instead has substituted as a more accurate test the question whether the method adopted for carrying on the enterprise most resembles that of an incorporated body."

2. In the opinion of the Board of Tax Appeals in the *Whitcomb Coca-Cola* case, the Board made the following statement in this connection:

   "But each must be decided upon its own facts. See particularly Morrissey v. Commissioner, 296 U. S. 344. The characteristics of alleged association must be compared with the characteristics typical of a corporation. If there is sufficient resemblance, then the taxpayer is held to be an association taxable as a corporation; but if there is little similarity, then the decision must be the other way."

consideration on its own peculiar facts. Here the decision below has held that the Board of Tax Appeals was correct in "its conclusion of law that respondent was not subject to income tax as a corporation." The decision below holds that the determination of the association issue depends upon whether the syndicate *resembles* a corporation more nearly than it does a partnership and that *this (resemblance) is a question of fact.* It is insisted that this conclusion is correct and not in conflict with any decision of this Court or with any decision of any other circuit.

The scope of review of the lower Court herein has not been so limited as to be in conflict with any other decision.

In this connection the case of *Commissioner v. Vandegrift Realty* Co., 82 F. (2d) 387 (C. C. A. 9th)[1] is cited in the petition. In the Vandegrift case as here, the peculiar facts were considered and the law applied.

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1. In the *Vandegrift* case the facts have no reasonable resemblance or analogy to the facts herein and among other things the Court said:

"We recognize that the question as to whether or not the trust engaged in business during a specified period is one of fact but we hold that it is a question of law as to the activity required in order that a trust be classified for tax purposes, either as an association or a simple, inactive, or pure trust, and we hold that it is a question of law, with respect to the measure or standard by which we may determine whether or not a trust shall be taxed as a corporation, by reason of its classificiation as an association."

In this connection the case of *Commissioner v Highlands E.-L. Subd., etc.*, 88 F. (2d) 355 (C. C. A. 7th)[1] certiorari denied, 302 U. S. 691, is cited in the petition. In the *Highlands* case as here the peculiar facts were considered and the law applied.

In this connection the case of *United States v. Trust No. B. 35*, 107 F. (2d) 22, (C. C. A. 9th)[2] is cited in the petition. In the Trust No. B. 1 case, as here, the peculiar facts were considered and the law applied.

In this connection the case of *Helvering v. Combs, 296 U. S. 365*, is cited in the petition. In the *Combs* case this Court considered the facts in detail, applied thereto the principles of law fixed in the case of *Morrissey v.*

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1. In the *Highlands* case, the Court among other things said:

> "In the Morrissey case the Court analyzed with great care the historical background of the various acts and regulations promulgated by the Treasury Department in the construction of the same, reviewed previous decisions, and established the general principles to be followed in the determination of whether, under a given state of facts, a trust is to be treated as a 'pure trust' or as an 'association' within the meaning of the act.
>
> "We need only say that a study of the facts in the instant case convinces us that they fall within the definition of an association as we gather it from those cases."

2. In this case in holding that there was an association

Commissioner, supra, and held that there was an association taxable as a corporation.

It is insisted that the conclusion of the Board of Tax Appeals in this case that respondent was not subject to income tax as a corporation is clearly correct and that no useful purpose may be served by granting the petition for certiorari. In this case there is a lack of practically all of the formalities and advantages of corporations and the attributes common to corporations are practically all lacking so that it cannot be said in any sense of the word that the attributes here involved have any reasonable resemblance or analogy to those of corporations. Whether the association issue in its final analysis be considered a question of fact or of law, it is insisted that each case must be decided upon its own peculiar facts and that if this respondent is to be held to be an association, then the rule will necessarily be so extended that each partnership and each joint venture and each joint ownership of property will constitute a group of persons subject to income tax as an association.

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taxable as a corporation, the Circuit Court said among other things:

"We hold that the trustee here was not administering a so-called 'traditional type of trust,' but a 'business trust' within Morrissey v. Commissioner, supra, conceived and intended to be conducted as a productive business enterprise for profit, and that it was in fact so conducted."

It is insisted that it was not the purpose of Congress to extend the burdens of corporation taxes to any taxable entities except corporations themselves and to regularly organized groups of individuals who, without a charter, conducted a regular business in the manner and form ordinarily used by corporations. *If the petitioner is desirous of extending this rule further, it is insisted that application should be made to the Congress to enact appropriate legislation in this connection.*

On page 18 of petition, the following statement is made as one of the reasons for granting the writ:

> "This case involves an issue of considerable importance in the administration of the income tax statutes. The question presented is a frequently recurring one, since the method of operation adopted by the parties interested in this lease is used extensively throughout the oil producing sections of the country. Many cases are pending before the Bureau of Internal Revenue, the Board of Tax Appeals, and the courts involving the same question with respect to similar joint undertakings. It is important, therefore, that this Court settle the application of established principles to this type of case."

It is agreed that the issue involved is one of considerable importance in the administration of the income tax statutes. The importance of the issue is clearly shown from the large number of cases litigated on this question. It is also admitted that the question is a frequently recurring one, but it is denied that the *method of operation* adopted by the parties interested in this lease is

used extensively throughout the oil producing sections of the country. This is said because it is difficult to find any number of cases involving this question with identical facts.

The question of depreciation is a frequently recurring one, but under our judicial system it is absolutely impossible for any court to lay down rules which will settle the many depreciation questions which have arisen and which, no doubt, will continue to arise in connection with the administration of the income tax laws.

It is denied that there are many cases pending before the Bureau of Internal Revenue, the Board of Tax Appeals and the Courts involving the same question with respect to *similar joint undertakings*. Two individuals and a corporation have simply sold interests in an oil and gas lease to each of several people under separate contract with each and have taken back from each a separate power of attorney making the sellers agents of each purchaser in the development and operator of the lease.

There are many cases involving the association question in connection with the operation of jointly owned oil properties, but the statement that there are many *similar joint undertakings* is challenged.

The principles govering the determination of the association issue in connection with the administration of income tax statutes have, it is urged, been clearly fixed by this Court, but, after all, the facts must be ascertained before the principles of law can be applied. Here

the facts are not considered to be in disupte and clearly in the *Morrissey* case, it is stated that the decision of the question is a matter of analogy—the determination of the issue as to whether or not the attributes present in a given case are sufficiently analogous to those of a corporation to justify the imposition of tax as a corporation.

CONCLUSION

Wherefore, it is respectfully submitted that the petition should be denied.

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Dallas, Texas,
July, 1940.

APPENDIX

Revenue Act of 1932, c. 209, 47 Stat. 169:

"SEC. 13. TAX ON CORPORATIONS

"(a) Rate of Tax.—There shall be levied, collected, and paid for each taxable year upon the net income of every corporation, a tax of 13¾ per centum of the amount of the net income in excess of the credit against net income provided in section 26."

* * *

"SEC. 52. CORPORATION RETURNS.

"(a) *Requirement.*—Every corporation subject to taxation under this title shall make a return, stating specifically the items of its gross income and the deductions and credits allowed by this title. The return shall be sworn by the president, vice president, or other principal officer and by treasurer or assistant treasurer. * * *

"SEC. 1111. DEFINITIONS.

"(a) When used in this Act—

"(1) The term 'person' means an individual, a trust or estate, a partnership, or a corporation.

"(2) The term 'corporation' includes associations, joint-stock companies, and insurance companies.

"(3) The term 'partnership' includes a syndicate, group, pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of this Act, a trust or estate or a corporation; and

the term 'partner' includes a member in such a syndicate, group, pool, joint venture, or organization.

* * *

"(6) The term 'fiduciary' means a guardian, trustee, executor, administrator, receiver, conservator, or any person acting in any fiduciary capacity for any person.

* * *

"(8) The term 'stock' includes the share in an association, joint-stock company, or insurance company.

"(9) The term 'shareholder' includes a member in an association, joint-stock company, or insurance company.

"SEC. 181. PARTNERSHIP NOT TAXABLE.

"Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity."

"SEC. 182. TAX OF PARTNERS

"(a) General Rule.—There shall be included in computing the net income of each partner his distributive share, whether distributed or not, of the net income of the partnership for the taxable year. If the taxable year of a partner is different from that of the partnership, the amount so included shall be based upon the income of the partnership for any taxable year of the partnership ending within his taxable year."

"SECTION 189. PARTNERSHIP RETURNS

"Every partnership shall make a return for each taxable year, stating specifically the items of its

gross income and the deductions allowed by this title, and shall include in the return the names and addresses of the individuals who would be entitled to share in the net income if distributed and the amount of the distributive share of each individual. The return shall be sworn to by any one of the partners."

"TREASURY REGULATIONS 77 PROMULGATED, under the Revised Act of 1932:

"ART. 1311. *Person*—The Act recognizes four classes of persons—individuals, trusts and estates, partnerships, and corporations. Corporations include associations, joint-stock companies and insurance companies, but not partnerships properly so called. A taxpayer is any person subject to a tax imposed by the Act.

"ART. 1312. *Association.* — Associations and joint-stock companies include associations, common law trusts, and organizations by whatever name known, which act or do business in an organized capacity, whether created under and pursuant to State laws, agreements, declarations of trust, or otherwise, the net income of which, if any, is distributed or distributable among the shareholders on the basis of the capital stock which each holds, or, where there is no capital stock, on the basis of the proportionate share or capital which each has or has invested in the business or property of the organization.

"ART. 1313. — *Association distinguished from partnership.*—An organization, the membership interests in which are transferable and the business of which is conducted by trustees or directors and officers without the active participation of all the members as such, is an association and not a part-

nership. The term 'partnership' includes a syndicate, group, pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of the Act, a trust or estate or a corporation; and the term 'partner' includes a member in such a syndicate, group, pool, joint venture, or organization. Organizations which have a fixed capital stock divided into shares represented by certificates transferable only upon the books of the company, which manage their affairs by a board of directors or executive officers, and which conduct their business in the general form and mode of corporations are joint-stock companies or associations within the meaning of the Act even though under State law such organizations are technically partnerships."

"ART. 1314. *Association distinguished from trust.*—Where trustees merely hold property for the collection of the income and its distribution among the beneficiaries of the trust, and are not engaged, either by themselves or in connection with the beneficiaries, in the carrying on of any business, no association exists, and the trust and the beneficiaries thereof will be subject to tax as provided by sections 161-170 and by articles 861-891. Where the trustees are not restricted to the mere collection of funds and their payment to the beneficiaries, but have similar or greater powers than the directors in a corporation for the purpose of carrying on some business enterprise, the trust is an association within the meaning of the Act."

"ART. 1320. *Fiduciary distinguished from agent.*— There may be a fiduciary relationship between an agent and a principal, but the word 'agent' does not denote a fiduciary. A fiduciary rela-

tionship cannot be created by a power of attorney. An agent having entire charge of property, with authority to effect and execute leases with tenants, entirely on his own responsibility and without consulting his principal, merely turning over the net profits from the property periodically to his principal by virtue of authority conferred upon him by a power of attorney, is not a fiduciary within the meaning of the Act. In cases where no legal trust has been created in the estate controlled by the agent and attorney, the liability to make a return rests with the principal."

"REVISED CIVIL STATUTES OF TEXAS

"ART. 5924. *Business under assumed name.*— No person shall conduct or transact business in this State under any assumed name or under any designation, name, style, corporate or otherwise other than the real name of each individual conducting or transacting such business, unless such person shall file in the office of the county clerk of the counties in which such person conducts, or transacts or intends to conduct or transact such business, a certificate setting forth the name under which such business is, or is to be, conducted or transacted, and the true full name or names of each person conducting or transacting the same, with the post office address of each. Said certificate shall be executed and duly acknowledged by the persons so conducting or intending to conduct said business in the manner provided for acknowledgement of conveyance of real estate.